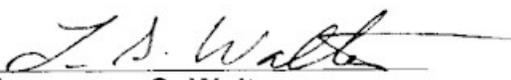


This document has been electronically entered in the records of the United States Bankruptcy Court for the Southern District of Ohio.

IT IS SO ORDERED.




Lawrence S. Walter
United States Bankruptcy Judge

Dated: June 01, 2010

**UNITED STATES BANKRUPTCY COURT
FOR THE SOUTHERN DISTRICT OF OHIO
WESTERN DIVISION AT DAYTON**

In re: SCOTT B. FORNSHELL
DIANE C. FORNSHELL,

Debtors.

Case No. 09-34005
Adv. No. 09-3239

GRAEME MAC KEOWN
VICTORIA MAC KEOWN,

Plaintiffs,

Judge L. S. Walter
Chapter 7

v.

SCOTT B. FORNSHELL,

Defendant.

**DECISION OF THE COURT DETERMINING STATE COURT JUDGMENT DEBT
OWED BY DEFENDANT-DEBTOR SCOTT FORNSHELL TO PLAINTIFFS GRAEME
AND VICTORIA MAC KEOWN TO BE DISCHARGEABLE IN BANKRUPTCY**

The court has jurisdiction over this matter pursuant to 28 U.S.C. §§ 157(a) and 1334, and the standing General Order of Reference in this District. This is a core proceeding pursuant to 28 U.S.C. §157(b)(2)(I).

This matter is before the court on the *Complaint for Nondischargeability of Debt under 11 U.S.C. § 523* [Adv. Doc. 1] filed by Plaintiffs Graeme and Victoria Mac Keown (the “Mac Keowns”) and the *Answer* filed by Defendant-Debtor Scott B. Fornshell (“Mr. Fornshell”) [Adv. Doc. 3]. In their complaint, the Mac Keowns ask the court to determine whether a debt owed to them by Mr. Fornshell is nondischargeable pursuant to 11 U.S.C. § 523(a)(2) and (6). They assert that the state court judgment obtained by them against Mr. Fornshell prior to his bankruptcy filing has a preclusive effect preventing Mr. Fornshell from relitigating some or all of the elements of nondischargeability at issue in this case.

The matter proceeded to trial on March 31, 2010. At trial, the Mac Keowns, through their counsel, stated their intent to abandon their cause of action pursuant to § 523(a)(6) for a willful and malicious injury. The court concurs with the Mac Keowns that § 523(a)(6) does not present a viable cause of action in this case given the facts presented to the court. Consequently, both the parties and this court focus on whether the debt is nondischargeable pursuant to the fraud exception found in § 523(a)(2).

The court has carefully considered and weighed the testimony of the witnesses, the exhibits admitted into evidence, and the closing arguments of counsel. The following decision constitutes the court’s findings of fact and conclusions of law in accordance with Fed. R. Bankr. P. 7052.

FACTS

This dispute is between the Mac Keowns, the purchasers of a new house, and the Debtor-Defendant, Mr. Fornshell, and his company, Fornshell Homes Ltd., the builder of that house. In

early May of 2003, the Mac Keowns first met with Mr. Fornshell at the house they eventually purchased. The house was a “spec” home, structurally completed but with finishing touches yet to be completed. Mr. Mac Keown is a mechanical engineer. Mrs. Mac Keown was formerly a high school and college math teacher and now works as a supervising editor and operations manager for a company that provides content for text books. Consistent with their educational and professional backgrounds, the Mac Keowns are very precise and exacting, careful of detail and language. At their first meeting with Mr. Fornshell they had many questions and requested copies of warranties, names of subcontractors, customer references, and other documentation, which Mr. Fornshell supplied. They were diligent in their physical examination of the property. They checked out all of the references and subcontractors and carefully read and re-read the one-page warranty policy as well as the lengthy industry standards manual.

In their review, the Mac Keowns noted that both the warranty policy and the industry standards manual referenced the Home Builders Association of Greater Cincinnati (“HBA”).

The warranty policy contained the following language:

All rights to the use of this Limited Warranty are reserved exclusively for members of the Home Builders Association of Greater Cincinnati who subscribe to its Code of Ethics. Copying or reproduction, in whole or in part, of this Limited Warranty is strictly prohibited.

Neither Mr. Fornshell nor his company was a member of the HBA and Mr. Fornshell made no other representations to that effect. However, the Mac Keowns interpreted these printed references to mean that Mr. Fornshell and his company were members of the HBA. This was their first purchase of a newly built house and they were comforted by the ostensible HBA representation because it imbued Mr. Fornshell with a certain professional status and also gave them some recourse to a third party arbitrator in the event of a dispute with the builder.

Mr. Fornshell has been a home builder for thirty years. His wife assists him in the business, particularly in sales. The Fornshells each have a high school education and are in some

respects less sophisticated than the Mac Keowns. For instance, when Mr. Fornshell and his company were later sued by the Mac Keowns and the Fornshells were unable to afford a lawyer, they failed to make an appearance and default judgment was entered against Mr. Fornshell because they did not know they could represent themselves without a lawyer. More importantly, Mr. Fornshell credibly testified that he obtained the HBA industry standards manual from a builder friend and simply provided it to home buyers without any thought as to its HBA origin. To him, having written building standards and principles available for customers was more important than the details contained in the documents; and the HBA reference was an irrelevance. Likewise, it was clear, although less explicit, that the warranties and other documentation supplied to the Mac Keowns were borrowed from other sources and not created by the Fornshells or an attorney on their behalf.

During the initial meeting with Mr. Fornshell, or shortly thereafter, Mr. Mac Keown questioned Mr. Fornshell about an apparent drainage problem on the property. Significant amounts of water flowed through the property creating a deep rut across the then unpaved driveway. When Mr. Mac Keown pointed out the drainage issue and voiced his concern that water might go over the top of the driveway, Mr. Fornshell responded that he intended to install drainage tile, a solution that appeared satisfactory to Mr. Mac Keown at the time.

The Mac Keowns contracted to purchase the house from Fornshell Homes Ltd. on May 27, 2003. The closing was on August 1, 2003. Mrs. Fornshell was present at the closing and provided the Mac Keowns with copies of the warranty and industry standards manual at that time. The warranty form was in a different format from the one provided by Mr. Fornshell during the May meeting. Mrs. Mac Keown testified that the industry standards manual was the same except that a line had been hand drawn through several provisions pertaining to water flow and drainage issues. The crossed out provisions were not discovered by Mrs. Mac Keown until

sometime after the closing. Mr. Fornshell denies crossing out provisions in the manual and no other witness or evidence was presented by the Mac Keowns as to the origin or effect of the apparent deletions.

After moving in, the Mac Keowns discovered a number of imperfections in their new house. Some of these problems, such as rain seeping under the back door, were rectified by Mr. Fornshell. Some, such as repair of damaged flooring in the kitchen, were not repaired to the satisfaction of the Mac Keowns. Still others were the subject of dispute, such as whether the builder was required to supply screens for windows on the detached garage. The most significant and costly remedial issue was the front drive drainage problem. However, even on this matter, the parties have very different views. The Mac Keowns insist that water should never flow over their driveway and point to the inadequate size of the drainage tile installed by the builder. Mr. Fornshell testified that a larger drainage tile would create an unsightly hump in the drive and that he intended that there be some overflow drainage during particularly heavy rains. As the one year anniversary of their purchase neared, the Mac Keowns sent a letter to Mr. Fornshell itemizing the items that needed immediate attention. Curiously, the drainage problem is not on the list.

In December of 2008, the Mac Keowns sued Mr. Fornshell and his company in an Ohio state court. Default judgment was rendered on February 5, 2009. A damages hearing was held at which Mr. Fornshell did not appear resulting in actual damages of \$17,156.25. That amount was trebled under the Ohio Consumer Sales Practice Act (O.R.C. § 1345.09(B)) to \$51,468.75, which, with the addition of costs, resulted in a final judgment of \$51,490.06 on February 24, 2009. Of the actual damages, \$13,400.00 related to the drainage issues.

Mr. and Mrs. Fornshell filed their Chapter 7 bankruptcy petition on June 30, 2009. On August 11, 2009, the Mac Keowns filed their adversary complaint against Mr. Fornshell seeking

a finding that the debt owed to them of \$51,490.06, plus interest, fees and costs, is nondischargeable in bankruptcy.

LEGAL ANALYSIS

A. Preclusive Effect of State Court Judgment

At the outset of the trial, the court outlined the limited preclusive effect of the state court default judgment that the Mac Keowns obtained against Mr. Fornshell prior to the bankruptcy filing, and the parties concurred with the court's view of the matter. However, this preliminary issue is of sufficient significance that the court will also address it here. First, pursuant to 28 U.S.C. § 1738, a federal court is to give the same preclusive effect to a state court judgment as another court of that state would give. *Sill v. Sweeney (In re Sweeney)*, 276 B.R. 186, 189 (B.A.P. 6th Cir. 2002) (citing *Markowitz v. Campbell (In re Markowitz)*, 190 F.3d 455, 461 (6th Cir. 1999)).

In Ohio, where the state court judgment against Mr. Fornshell was entered, there are two preclusionary principles that could apply: issue preclusion, also called collateral estoppel, and claim preclusion, also called res judicata.

Issue preclusion is generally raised when a party wants to use specific findings and conclusions in a state court's determination to preclude relitigation of the same findings or conclusions that are relevant to a subsequent but different cause of action between the same parties. *See Markowitz*, 190 F.3d at 461. An example would be a fraud judgment in state court and the use of issue preclusion to preclude the relitigation of identical elements during a nondischargeability proceeding in bankruptcy court. *Grogan v. Garner*, 498 U.S. 279, 284-85 (1991). However, one of issue preclusion's requirements in Ohio is that the issue in state court be "actually litigated." *Sweeney*, 276 B.R. at 192-94. Since default judgments generally do not

involve actual litigation of specific issues, issue preclusion cannot be applied when the state court judgment is a true judgment by default. *Id.* at 194.

However, that does not mean that a prior default judgment has no effect in bankruptcy court. A final state court judgment conclusively establishes the amount and liability for the creditor's underlying claim against the debtor. If those matters are fully and finally decided by the state court, even if by default judgment, they cannot be revisited or set aside by the bankruptcy court pursuant to the doctrines of claim preclusion and Rooker-Feldman.

Under Ohio's doctrine of claim preclusion, a final judgment rendered by a court of competent jurisdiction is conclusive as to the rights of the parties and their privies and constitutes an absolute bar to a subsequent action involving the same claim or cause of action. *Sliva v. May (In re May)*, 321 B.R. 462, 466 (Bankr. N.D. Ohio 2004) (citing *Holzember v. Urbanski*, 86 Ohio St.3d 129, 132, 712 N.E.2d 713 (1999)). Unlike the doctrine of issue preclusion, claim preclusion does not require that the matter be actually litigated as long as the defendant had a full and fair opportunity to litigate. *May*, 321 B.R. at 466. Consequently, claim preclusion generally prevents a bankruptcy court from re-evaluating a state court judgment finding a debtor liable for damages even if it is a judgment by default. *Id.*

The doctrine of Rooker-Feldman also prevents a bankruptcy court from entertaining a collateral attack against a final state court judgment. Rooker-Feldman prevents a losing party in a state court proceeding from asking a lower federal court to entertain an appeal of the state court judgment. *Exxon Mobil Corp. v. Saudi Basic Indus. Corp.*, 544 U.S. 280, 284 (2005) (noting that it prevents: “. . . cases brought by state court losers complaining of injuries caused by state court judgments rendered before the district court proceedings commenced and inviting district court review and rejection of those judgments”). *See also Singleton v. Fifth Third Bank of Western Ohio (In re Singleton)*, 230 B.R. 533, 536-39 (B.A.P. 6th Cir. 1999) (providing an

analysis of the differences between preclusionary principles and Rooker-Feldman); *May*, 321 B.R. at 466-67.

The application of these doctrines in this case leads to this result: the Mac Keowns cannot use issue preclusion and the default judgment to establish the elements of nondischargeability pursuant to § 523 because these elements were not actually litigated in state court. Consequently, the Mac Keowns are required to establish the elements of their nondischargeability cause of action through the testimony and evidence presented during the trial. However, the default judgment conclusively determines Mr. Fornshell's liability for the debt to the Mac Keowns and the amount of that debt.

B. Nondischargeability Claim Pursuant to § 523(a)(2)(A)

The Mac Keowns request a determination that the debt owed by Mr. Fornshell is nondischargeable pursuant to 11 U.S.C. § 523(a)(2), a statute pertaining to debts arising from fraudulent misrepresentations, false pretenses or actual fraud. They assert that Mr. Fornshell misrepresented his membership in the Home Builders Association of Greater Cincinnati by presenting them with an industry standards manual and a warranty policy that included a statements that the documents were only to be used by HBA members.

Because the allegedly false statement is not a statement about Mr. Fornshell's finances,¹ the applicable subsection is § 523(a)(2)(A) which states as follows:

(a) A discharge under section 727 . . . of this title does not discharge an individual debtor from any debt—

(2) for money, property, services, or an extension, renewal, or refinancing of credit, to the extent obtained by—

(A) false pretenses, a false representation, or actual fraud, other than a statement respecting the debtor's or an insider's financial condition[.]

¹ Fraudulent statements pertaining to a debtor's financial condition are dealt with separately in § 523(a)(2)(B).

1 U.S.C. § 523(a)(2)(A). “In order to promote the fresh start policy of the Bankruptcy Code, this exception to discharge is strictly construed against the creditor.” *Schafer v. Rapp (In re Rapp)*, 375 B.R. 421, 429 (Bankr. S.D. Ohio 2007). Indeed, “[i]f there is room for an inference of honest intent, the question of nondischargeability must be resolved in favor of the debtor.” *Id.* (further citations omitted).

In order to except a debt from discharge under § 523(a)(2)(A), a creditor must prove:

. . . (1) the debtor obtained money through a material misrepresentation that, at the time, the debtor knew was false or made with gross recklessness as to its truth; (2) the debtor intended to deceive the creditor; (3) the creditor justifiably relied on the false representation; and (4) its reliance was the proximate cause of loss.

Rembert v. AT&T Universal Card Services, Inc. (In re Rembert), 141 F.3d 277, 280-81 (6th Cir. 1998). The Mac Keowns, as the plaintiffs, carry the burden of proving the elements by a preponderance of the evidence. *Id.* at 281.

The first element that the Mac Keowns must prove is that a “material misrepresentation” was made by Mr. Fornshell. *Rembert*, 141 F.3d at 280-81. In this case, the Mac Keowns assert that Mr. Fornshell misrepresented that he had membership in the Home Builders Association of Greater Cincinnati. However, the facts establish that Mr. Fornshell never expressly stated to the Mac Keowns that he was a member of the HBA. Nor, for that matter, did the Mac Keowns ask the question. Instead, the Mac Keowns argue that Mr. Fornshell’s presentation of a pre-printed warranty and industry standards manual from the HBA with a statement on the warranty that it was only to be used by HBA members created the impression that Mr. Fornshell was, in fact, a member of the HBA. Consequently, the Mac Keowns actually allege a “false pretense” rather than an express misrepresentation.²

² Although the factual allegation is notably absent from their complaint, the Mac Keowns asserted at trial that another fraudulent misrepresentation was made by Mr. Fornshell when he allegedly crossed out certain provisions pertaining to drainage and water issues in the industry standards manual presented by his wife at the closing. Mrs. Mac Keown testified that she discovered the deletions sometime after the closing. She testified that these deletions were not disclosed at the closing nor were these deletions in the original manual provided to the Mac Keowns before

A “false pretense” is an “implied misrepresentation or conduct which creates and fosters a false impression” and it can form the basis for a nondischargeable debt pursuant to 11 U.S.C. § 523(a)(2)(A). *Stevens v. Antonious (In re Antonious)*, 358 B.R. 172, 182 (Bankr. E.D. Penn. 2006). *See also Rapp*, 375 B.R. at 435 (describing false pretenses as a “‘mute charade,’ where the debtor’s conduct is designed to convey an impression without oral representation”). However, a false pretense must be “fostered willfully, knowingly, and by design; it is not the result of inadvertence.” *Antonious*, 358 B.R. at 182. *See also McLeod v. Barnaby (In re Barnaby)*, 2007 WL 750332, at *2 (Bankr. D. N.J. March 6, 2007) (the elements needed to establish a false pretense include an implied misrepresentation or conduct by the defendant promoted knowingly and willingly).

The court recognizes that Mr. Fornshell’s use of the HBA’s model warranty and industry standards manual may have been somewhat disingenuous. However, the court finds a complete lack of evidence to support that Mr. Fornshell knowingly and willfully used the documents to foster an impression that he was, in fact, a member of the HBA. Mr. Fornshell credibly testified at the trial that he had been in the home construction business for thirty years and, over time, had grown disenchanted with the one page warranty he had been providing to his customers. It is unclear from the testimony whether the original warranty or warranties used by Mr. Fornshell were borrowed from the HBA, but it is clear that Mr. Fornshell was in the habit of adopting forms used by others in the trade rather than creating them from scratch. In any event, sometime prior to the transaction with the Mac Keowns, he adopted the HBA’s warranty and industry standards manual provided to him by a builder friend to enhance his paperwork offerings. He began providing them to all of his customers, including the Mac Keowns. The fact that the

they entered the contract with Mr. Fornshell. At trial, Mr. Fornshell denied crossing out the provisions. Besides Mrs. Mac Keown and Mr. Fornshell, no other witness was questioned about these deletions nor was any other evidence presented regarding how the deletions occurred or who might have made them. Consequently, the evidence is in equipoise. The court concludes that the preponderance of the evidence does not establish that these deletions were the work of Mr. Fornshell.

documents came from the HBA and contained language limiting their use to HBA members was irrelevant to Mr. Fornshell. He just wanted to give his customers a more detailed explanation of the standards and procedures to which he personally adhered and found the HBA documents to fit the bill.

The court believes that if the Mac Keowns had asked Mr. Fornshell whether he was a member of the HBA, he would have truthfully told them that he was not and never had been a member. As noted before, however, they did not ask. While they carefully questioned Mr. Fornshell and his wife about the home and the transaction they were going to enter and diligently checked his references, Mr. Fornshell's potential membership in the HBA was not of sufficient importance to the Mac Keowns to question.

Certainly it is true that knowing and willful misrepresentations, whether express or implied, about a builder's qualifications intended to induce customers to enter into a transaction and pay out money have resulted in nondischargeable debts pursuant to 11 U.S.C. § 523(a)(2)(A). *See Gem Ravioli, Inc. v. Creta (In re Creta)*, 271 B.R. 214, 220-21 (B.A.P. 1st Cir. 2002) (listing cases). *See also Antonious*, 358 B.R. at 183-84; *Kadlecek v. Ferguson (In re Ferguson)*, 222 B.R. 576, 585-86 (Bankr. N.D. Ill. 1998). However, this is not such a case. Although the Mac Keowns may have received the incorrect impression that Mr. Fornshell was a member of the HBA through his presentation of the HBA's warranty and industry standards manual, he never expressly stated as much nor did he knowingly and willfully create that impression by using the documents. Furthermore, their reliance on such an impression is questionable given that the documents do not actually state that Mr. Fornshell is a member of the HBA and the Mac Keowns never bothered to question him about it.

Ultimately, this case falls into the same category as many others involving a dispute between a purchaser disappointed by the imperfections in a new home, remodeling job or other

construction and a contractor frustrated by the demands of the customer. *See, e.g., Strominger v. Giquinto (In re Giquinto)*, 399 B.R. 152 (Bankr. E.D. Penn. 2008); *Aiken v. Reynolds (In re Reynolds)*, Adv. No. 07-1014, adv. doc. no. 25 (Bankr. S.D. Ohio May 20, 2008) (J. Aug); *Siebanoller v. Rahrig (In re Rahrig)*, 373 B.R. 829 (Bankr. N.D. Ohio 2007); *LeDoux v. Tanner (In re Tanner)*, 365 B.R. 217 (Bankr. N.D. Ala. 2007); *Bohannon v. Horton (In re Horton)*, 372 B.R. 349 (Bankr. W.D. Ky. 2007); *Barnaby*, 2007 WL 750332; *Rezin v. Barr (In re Barr)*, 194 B.R. 1009 (Bankr. N.D. Ill. 1996). While the facts in many of these cases may present a breach of contract claim, they do not rise to the level of dishonesty or fraud.

In conclusion, the facts do not establish, by a preponderance of the evidence, that Mr. Fornshell knowingly and willfully misrepresented his membership in the Home Builders Association of Greater Cincinnati. The court concludes that the debt owed by Mr. Fornshell to the Mac Keowns is dischargeable in his bankruptcy case. All relief requested in the Plaintiffs' complaint is denied.

SO ORDERED.

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